



HAN KUN LAW OFFICES

# Legal Commentary



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## Private Equity Law

### **Introduction to the *Interim Measures on Carrying Out the Pilot Program for Foreign-Invested Equity Investment Enterprises and Management Enterprises in Tianjin* and Its Implementing Rules**

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After the Shanghai and Beijing Municipal Governments successively promulgated the rules for pilot foreign-invested equity investment enterprises, Tianjin Development and Reform Commission (“**Tianjin DRC**”), Financial Affairs Office of Tianjin Municipal People’s Government, Tianjin Commission of Commerce and Tianjin Administration for Industry and Commerce jointly issued the *Interim Measures on Carrying out the Pilot Program for Foreign-Invested Equity Investment Enterprises and Management Enterprises in Tianjin* (the “**Tianjin QFLP Measures**”) and the *Implementing Rules on the Interim Measures on Carrying out the Pilot Program for Foreign-Invested Equity Investment Enterprises and Management Enterprises in Tianjin* (the “**Implementing Rules**”) on October 14, 2011. The Tianjin QFLP Measures will come into force as of the date of promulgation, while the Implementing Rules will take effect 30 days thereafter.

The Tianjin QFLP Measures and the Implementing Rules mainly regulate the establishment, fundraising and downstream investment, risk control, information disclosure and filing for foreign-invested equity investment funds and foreign-invested fund management enterprises. The Tianjin QFLP Measures and the Implementing Rules were generally modeled after the QFLP measures issued in Shanghai and Beijing, with some differences with respect to foreign exchange settlement, qualifications for pilot equity investment management enterprises and other aspects.

## 1. Competent Governmental Authority for the Pilot Program

Tianjin Municipal Office for Development of Industry (Equity) Investment Funds and Administration of Filing (the “**Municipal Filing Office**”), which consists of Tianjin DRC, Tianjin Commission of Commerce, the Municipal Financial Office, Tianjin Administration for Industry and Commerce, Tianjin Municipal Finance Bureau, Tianjin Tax Bureau, Tianjin Banking Regulatory Bureau and Tianjin Private Equity Association, is the competent governmental authority for administering the Pilot Program. A pilot enterprise will be recognized upon the approvals by the Municipal Filing Office and leaders of Tianjin Municipal Government.

## 2. Recognition of Pilot Enterprises

The pilot enterprises refer to foreign-invested equity investment enterprises and foreign-invested management enterprises as recognized by the Municipal Filing Office, which will generally take two procedures (i.e., examination and approval).

**Examination** Equity investment enterprises and management enterprises applying for the pilot program shall submit relevant materials through the equity investment management enterprises to Tianjin DRC, who shall call the members of the Municipal Filing Office to review the application, which is expected to be finished within ten (10) business days upon receipt of the complete application documents.

**Approval** Equity investment enterprises and management enterprises passing the examination shall submit relevant materials through the equity investment management enterprises to Tianjin DRC, who shall convene the members of the Municipal Filing Office to review the qualifications for the pilot program and the foreign exchange settlement quota within ten (10) business days upon receipt of the complete application documents. Enterprises qualified for the pilot program after the review process shall be reported by Tianjin DRC to competent municipal leaders for approval, and Tianjin DRC shall issued verification documents to the applying enterprises after such approval.

## 3. Qualifications for Pilot Enterprises

### **Qualifications for Pilot Foreign-Invested Equity Investment Management Enterprises**

According to the Tianjin QFLP Measures and the Implementing Rules, qualifications for a pilot equity investment management enterprise include that the following: (i) the business scope stipulated in the articles of association or the partnership agreement shall be limited to establishment of equity investment enterprises, management of the assets of equity investment enterprises, provision of management services for portfolios of equity investment enterprises, equity investment consultation, or other activities related to equity investment;

(ii) the paid-in capital shall be no less than RMB10 million or equivalent amount of foreign currency; (iii) it has at least two (2) senior management personnel satisfying all of the following requirements: (A) more than five (5) years of experience in the business of equity investment or equity investment management; (B) more than two (2) years of experience in a position of senior management; (C) experience in China-related equity investment or work experience in Chinese financial institutions; (D) no record of violation of laws and regulations within the recent five (5) years or pending economic disputes, plus a record of good personal credit; (iv) it has law/rule-compliant operation, strict and reasonable investment decision procedures and risk control system; (v) it has a sound internal finance management system and accounting measures in accordance with applicable finance and accounting rules; and (vi) the equity investment enterprises to be raised or managed by it shall primarily invest in the new industries preferentially developed in Tianjin (Unlike Beijing, *Tianjin does not enumerate the specific industries. Based on our telephone inquiry on a no name basis, the official of Tianjin DRC indicated that there is no specific industry investment restriction, but applications from the equity investment enterprises that can demonstrate a pipeline of projects in Tianjin will be preferred*).

It is noteworthy that the paid-in capital of equity investment management enterprises participating in the pilot program shall be no less than RMB10 million or equivalent amount of foreign currency. In comparison, the registered capital requirement for the pilot management enterprises to be established in Shanghai is no less than USD2 million, while no clear requirement has been set forth in Beijing. The Tianjin QFLP Measures further require that the pilot equity investment management enterprises shall have certain senior Chinese management personnel, while no similar requirements were provided in Beijing QFLP measures or Shanghai QFLP measures.

***Qualifications for Pilot Foreign-Invested Equity Investment Enterprises*** According to the Tianjin QFLP Measures and the Implementing Rules, qualifications for a pilot foreign-invested equity investment enterprise include that the following: (i) it may consist solely of foreign capital raised offshore, or partially of RMB funds raised onshore and partially of foreign capital raised offshore, and the total size of the fund shall in principle be no less than RMB500 million or equivalent amount of foreign currency. The equity investment management enterprise can subscribe for certain percentage (no more than 5%) of the investors' total capital commitments to the fund; (ii) its management enterprise shall be qualified as a pilot equity investment management enterprise as set forth above; and (iii) its offshore investors shall meet the following requirements: (A) during the preceding fiscal year, its own assets shall be no less than USD500 million or the assets under its management shall be no less than USD1 billion; (B) it shall have a sound governance and internal control system and shall not have been subject to any sanction by onshore judicial departments or relevant supervision organizations within the most recent two (2) years; (C) it shall be mainly comprised of offshore sovereign wealth funds, pension funds, endowment funds, charitable

foundations, fund of funds, insurance companies, banks, security companies and other offshore institutional investors recognized by the Municipal Filing Office; (D) each offshore investor shall subscribe for at least USD10 million in the pilot equity investment enterprise; and (E) the offshore investor or its affiliates shall have more than five (5) years of relevant investment experience.

It is provided that no upper limit on foreign capital is set for pilot equity investment enterprises (i.e., the fund can be comprised solely of foreign capital), reflecting an open attitude of Tianjin toward introducing foreign capital. Meanwhile, the size of pilot equity investment enterprises in Tianjin is required to be no less than RMB500 million or equivalent amount of foreign currency, which is consistent with that in Beijing but much higher than the USD15 million required in Shanghai. In addition, as to the minimum capital commitment for offshore investors, the Tianjin QFLP Measures state the minimum requirement of USD10 million, which is higher than that for limited partners of pilot enterprises in Shanghai (i.e., USD1 million).

#### **4. Investment by Pilot Enterprises**

A pilot equity investment management enterprise is allowed to settle foreign capital with its custodian bank according to applicable foreign exchange regulations, and further makes capital commitment to the equity investment enterprise established by it. Such capital contribution by pilot equity investment management enterprise will not affect the nature of the equity investment enterprise invested by it. The amount of foreign capital settlement by a pilot equity investment management enterprise is limited to 5% of the paid-in capital (including accumulative amount of settled capital) of the equity investment enterprise, which is generally consistent with the QFLP measures in Beijing and Shanghai.

In addition, the Tianjin QFLP Measures and the Implementing Rules impose following investment prohibitions on pilot enterprises: no investment in industries where foreign investments are prohibited; no secondary securities transactions; no financial derivatives transactions; no non-self-use real estate investment; no use of proprietary funds to make investments; no provision of loans or guarantees to any third party; and no engagement in other activities prohibited by applicable law or the articles of association (or the partnership agreement) of the equity investment enterprises.

#### **5. Fund Custody and Foreign Exchange Settlement for Pilot Enterprises**

According to the Tianjin QFLP Measures and the Implementing Rules, pilot enterprises shall entrust the head office or the branch office of a commercial bank that satisfies relevant requirements and conditions as the custodian bank. In addition, pilot equity investment enterprises shall open several accounts with its custodian bank, including (i) a designated

foreign exchange account (foreign capital account for legal person enterprises and designated foreign capital account for non-legal person enterprises), to accept capital contributions by offshore investors; (ii) a designated investment account, to collectively manage the settled capital of the pilot equity investment enterprise and its investment; and (iii) a designated proceeds account, to collect investment proceeds and other earnings. Pilot equity investment enterprises with onshore investors shall open an RMB settlement account to accept capital contributions of the onshore investors.

In addition, the foreign capital settlement for a pilot enterprise shall be based on the actual need of its investment (i.e., within the upper limit on foreign capital settlement, pilot enterprises will only be allowed to settle its foreign capital for the amount actually needed for its impending investments). According to the Implementing Rules, the investment made by pilot equity investment enterprises using its settled capital shall be regarded as foreign direct investment, which requires prior approval from local DRC and Commission of Commerce where the target company is located. After the verification and check by Tianjin Administration of Foreign Exchange, pilot equity investment enterprises may, within its settlement limit, apply to its custodian bank for foreign capital settlement in accordance with its investment schedule. The settled capital shall be put in the designated investment account and shall be used within seven (7) business days after the RMB capital and foreign capital have been collected at the percentage agreed upon at the registration. Otherwise, the qualification of the pilot enterprise will be revoked.

We note from the aforesaid provisions that compared to the Beijing and Shanghai QFLP regulations, the Tianjin regulations impose more detailed and comprehensive requirements for foreign capital settlement, and exercise a stricter scrutiny over the investment activities of foreign-invested equity investment enterprises.

Han Kun Fund Formation & Management Group has first hand experience representing fund clients in handling QFLP applications in different cities. Should you have any questions regarding the above, please do not hesitate to contact us.

## **Important Announcement**

This Legal Commentary has been prepared for clients and professional associates of Han Kun Law Offices. Whilst every effort has been made to ensure accuracy, no responsibility can be accepted for errors and omissions, however caused. The information contained in this publication should not be relied on as legal advice and should not be regarded as a substitute for detailed advice in individual cases.

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